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A Monthly Report from The Conference Board

INTERNATIONAL ECONOMIC SCOREBOARD

The Conference Board

DECEMBER, 1986

SUMMARY

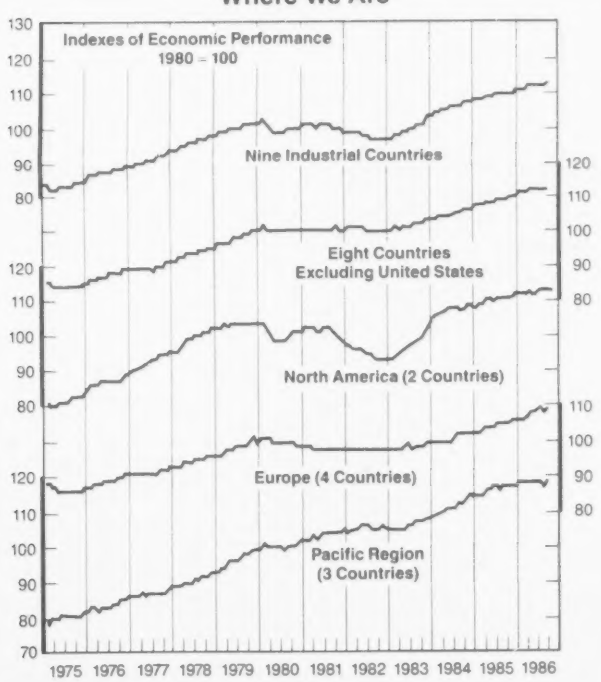
The world business expansion is gaining momentum. In the United Kingdom and Australia the leading indexes have switched direction from decline to growth. In the United States, Japan and France, the leaders have strengthened further. This concerted action has brought the growth rate of the nine-country index to 7 percent, the fastest since early 1984. Taiwan, R.O.C., remains the star performer, with its leading index growth rate hitting 14 percent.

The economic performance indexes are moving ahead at a more modest pace but, in view of the good news from the leading indexes, faster economic growth should be reported before long. Each country can look forward to the gains promised by its own leading index, and also to some stimulus derived from the improvement taking place abroad. Under these conditions, the industrial world's expansion is self-reinforcing.

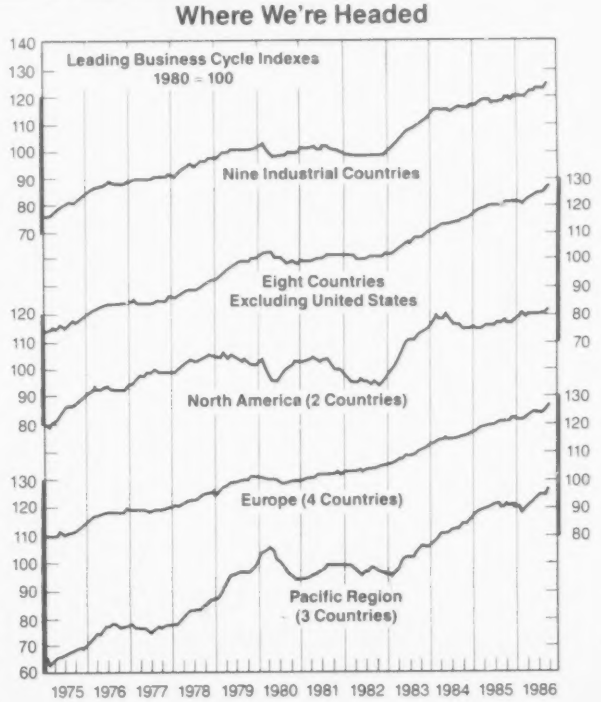
	Ten-year Growth	Indexes of Economic Performance Growth Rates*			Leading Business Cycle Indexes Growth Rates*				
	Rate 1969-79	6 mos. ago	3 mos. ago	Latest month	6 mos. ago	3 mos. ago	Latest month	Current Reading on the Cycle	Latest Month Covered
	annual rates, percent								
9 countries	4	3	3	3	2	4	7	Expansion continuing	Sept.
8 countries ex. U.S.	4	3	3	3	2	5	7	Expansion continuing	Sept.
North America (2)	3	2	2	3	3	3	5	Expansion continuing	Sept.
Europe (4)	3	3	4	4	4	5	7	Expansion continuing	Sept.
Pacific Region (3)	5	2	2	1	-2	6	8	Expansion stalling, leaders strong	Sept.
United States	3	4	3	3	4	3	6	Expansion continuing	Oct.
Canada	4	3	2	1	4	3	3	Expansion continuing	Sept.
West Germany	3	4	7	6	3	6	4	Expansion continuing	Sept.
France	4	4	4	4	5	7	11	Expansion continuing, leaders strong	Sept.
United Kingdom	2	2	2	2	1	-1	4	Expansion continuing	Sept.
Italy	3	1	3	-1	10	9	8	Expansion stalling, leaders strong	Aug./Sept.
Japan	5	2	1	1	-2	7	9	Expansion stalling, leaders strong	Sept.
Australia	4	5	5	1	-7	-2	3	Expansion stalling, leaders reviving	Sept.
Taiwan, R.O.C.	10	7	9	10	13	13	14	Expansion continuing, leaders strong	Oct.

* Ratio of current month's index over the preceding 12 months, expressed as a compound annual rate.

Where We Are


Indexes of Economic Performance
1980 = 100
Nine Industrial Countries
Eight Countries Excluding United States
North America (2 Countries)
Europe (4 Countries)
Pacific Region (3 Countries)
1975 1976 1977 1978 1979 1980 1981 1982 1983 1984 1985 1986

Where We're Headed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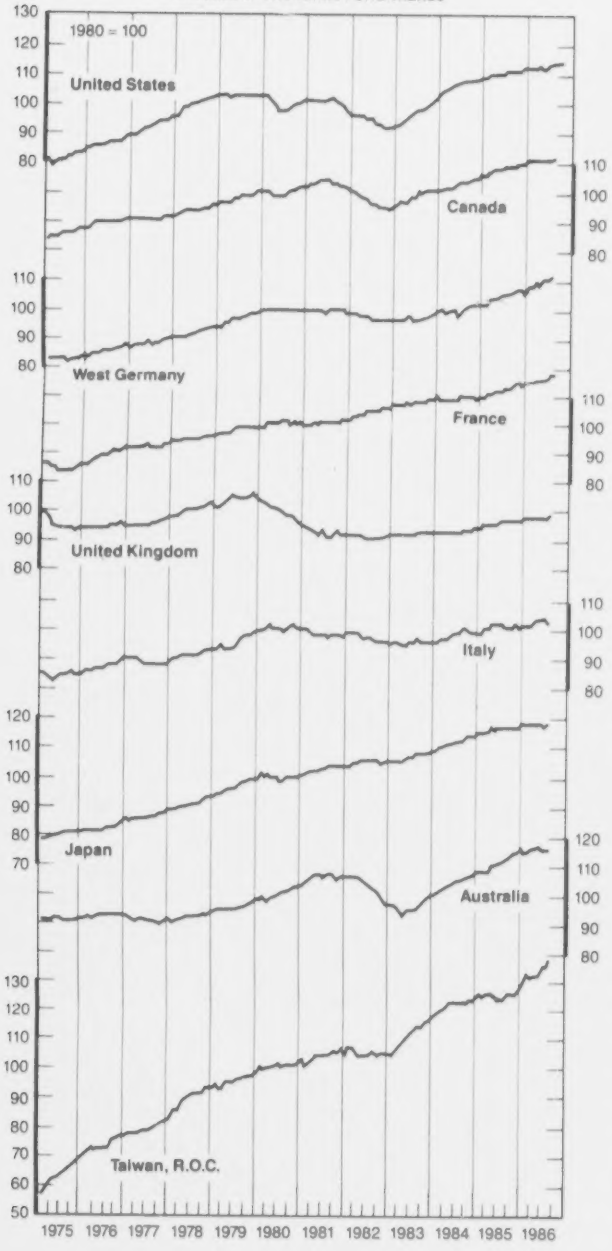
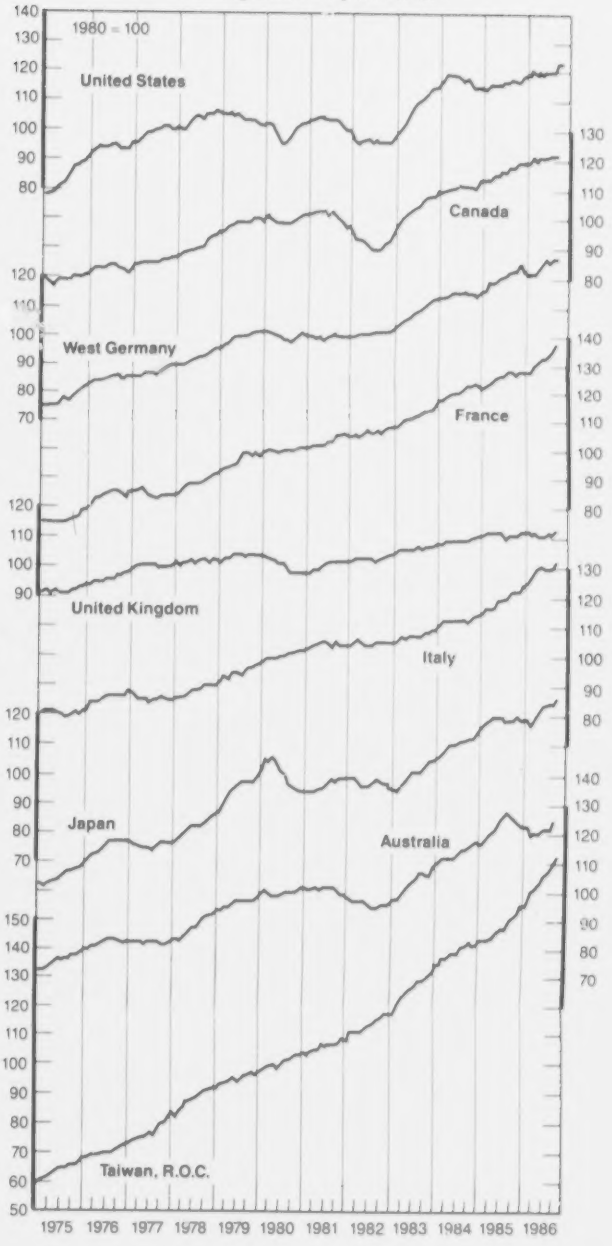
Where We Are

Indexes of Economic Performance



Where We're Headed

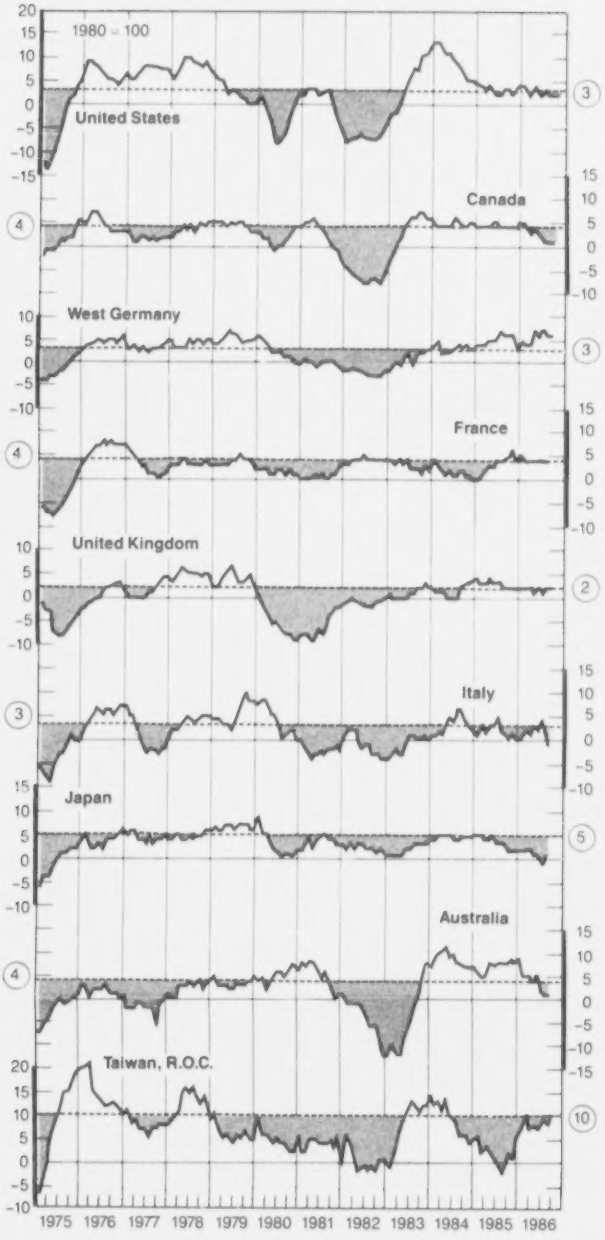
Leading Business Cycle Indexes



Sources: CIBCR and The Conference Board

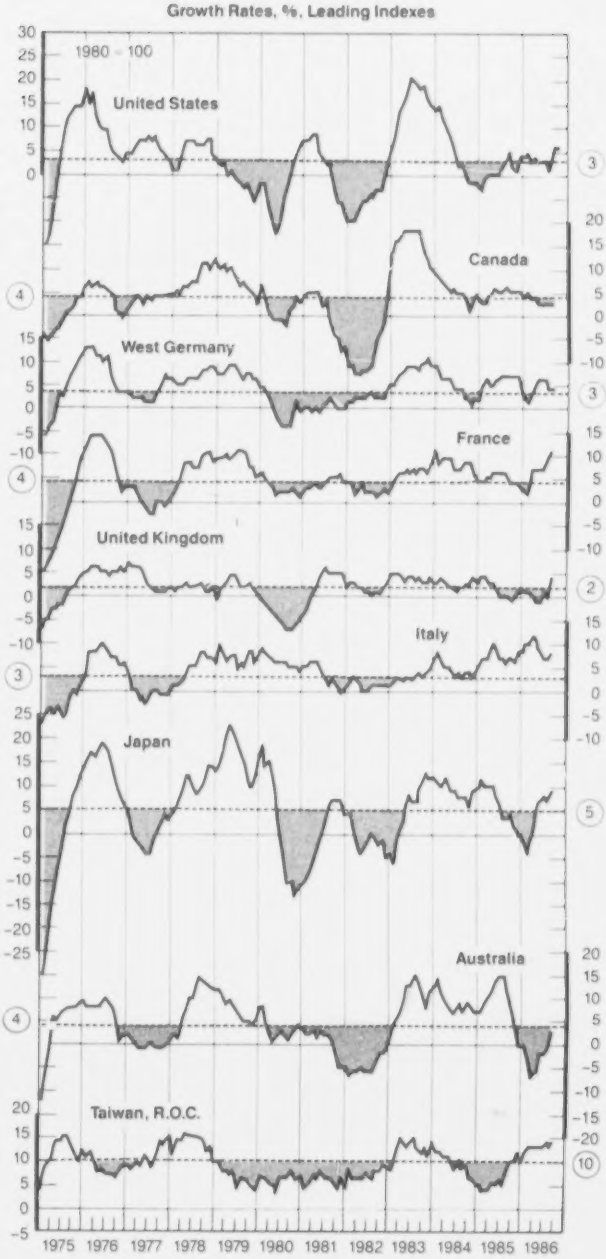
Where We Are

Growth Rates, %, Performance Indexes



Where We're Headed

Growth Rates, %, Leading Indexes



Note: Horizontal dashed lines are average rates for 1969-79 in the index and in Real GNP

Sources: CIBCR and The Conference Board

PROSPECTS FOR GROWTH IN U.S. EXPORTS: BEST IN TEN YEARS

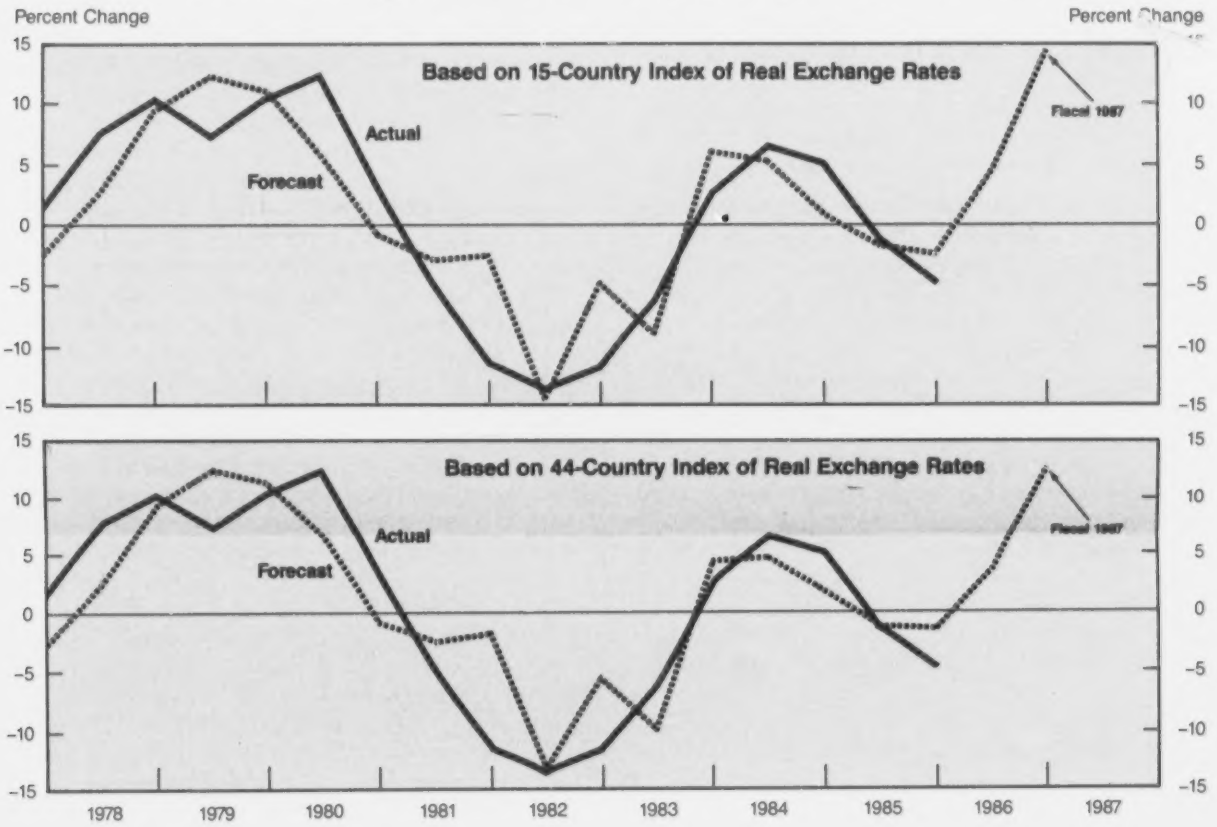
The imbalance between U.S. exports and imports has widened dramatically in recent years. At the start of the economic expansion in late 1982 the trade deficit (goods and services) was about $15 billion (annual rate). Since then imports have skyrocketed by about $150 billion, while our exports have increased by only $40 billion. The result is a worrisome deficit of some $125 billion.

The steep increase in imports in 1983 and 1984 was doubtless tied to the substantial economic recovery in the U.S. during that period. Real GNP grew by 3.5 percent in 1983 and 6.5 percent in 1984. In contrast, growth in real output in the European community was 1.2 percent in 1983 and 2.1 percent in 1984. In the developing economies output growth amounted to 0.4 percent and 2.1 percent in the same years. This anemic growth outside the U.S. thwarted the growth of U.S. exports, and the very fast expansion here created a large demand for foreign goods.

The sharp rise in the foreign exchange value of the U.S. dollar from the early 1980s through the start of 1985 also blunted the physical growth of U.S. exports and stimulated imports. According to the widely-cited Federal Reserve Board's 10-country exchange rate index, the dollar rose close to 80 percent from 1980 to the first quarter of 1985. During the same period, export prices rose 14 percent, while import prices fell 1 percent.

Since then there has been a substantial reversal in the dollar exchange rate. The 10-country dollar exchange in-

Forecast and Actual Changes in Real Volume of U.S. Exports of Manufactured Goods



Source: Center for International Business Cycle Research.

dex dropped about one-third and import prices, excluding oil, have begun to rise much more rapidly than export prices. These changes enhance the competitiveness of American goods in international markets. Not only that, but the *Scoreboard's* indexes of economic performance show that since 1984 the U.S. growth rate has slackened relative to the growth rates in most other countries. From these developments it would be easy to reach the rosy conclusion that the U.S. trade deficit should have fallen considerably in 1986. Alas, although there has been some decline in the deficit the past few months, the gap between exports and imports still remains very wide.

In an effort to account for the persistent deficit, numerous studies in recent months have sought to develop alternative measurements of the exchange value of the U.S. dollar. These alternative measures make use of wider coverage, different trade weights, and often involve deflation of the nominal exchange values to obtain real exchange rates. The studies recognize that trade with the major industrialized economies is becoming relatively less important. Countries in the Pacific Basin and Latin America are now playing a bigger role in U.S. trade. Moreover, deflation of the nominal exchange rates is needed to take account of inflation rate differentials between the U.S. and its important trade partners.

In this issue of the *Scoreboard* we use these exchange-rate series in conjunction with our own data on economic activity abroad to assess prospects for the growth in the real volume of U.S. manufactured goods exports in the months immediately ahead. Two alternative indexes of real dollar exchange rates constructed by Morgan Guaranty are used. One covers 15 major industrial countries; the other includes an additional 29 countries, or 44 countries in all. To guage demand from abroad, we use the *Scoreboard's* 8-country leading index, since this forecasts future changes in the growth of output in important industrial economies outside the U.S., and hence the demand for our exports.

Specifically, suppose we want to forecast the change in the volume of U.S. manufactured exports from the year ending last June to the year ending next June. The explanatory variables employed in this exercise are the growth rate in the 8-country leading index for June 1986 and the percentage change in the real foreign exchange value of the U.S. dollar as of January 1986. To forecast the calendar year change in exports, 1986 to 1987, the leading index growth rate would be for December 1986 and the exchange rate change would be for June 1986. This allows for roughly a six-month lead in the leading index and a twelve-month lead in the exchange rate, vis-a-vis exports.

Correlation coefficients (R^2) testing this relationship from 1978 through mid-1986 are fairly high, accounting for nearly three-fourths of the variability in the yearly changes in manufactured goods exports. Interestingly, it makes little difference which of the two exchange rate indexes is used. That is to say, when exchange rates are expressed in real terms, the inclusion of the smaller countries has little effect on the movement of the index. Between February 1985 and August 1986, for example, the 15-country real exchange rate index dropped 25 percent, while the 44-country index fell 21 percent.

The accompanying chart shows the percent changes in the actual and forecast volumes of U.S. manufactured exports from 1978 through fiscal 1987, and suggests that a major improvement in the huge trade deficit is on the way. The forecast derived by using the 8-country leading index along with the 15-country real dollar exchange index is for a 14.5 percent increase in the quantity of U.S. manufactured exports from fiscal 1986 to fiscal 1987. When the 44-country exchange rate index is used instead of the 15-country index it appears that a 12.5 percent rise is in the works.

U.S. exporters would be happy with either outcome and so too would American workers in the export industries. U.S. economic policymakers should also be able to manage a few smiles.

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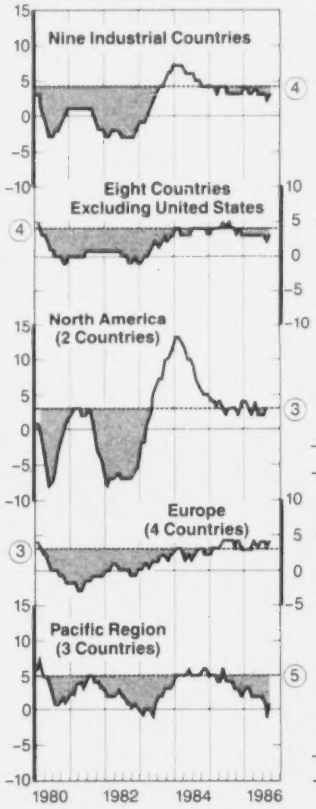
INDEXES, NINE COUNTRIES, 1985-86

		U.S.		Canada		West Germany		France		U.K.		Italy		Japan		Australia		Taiwan, R.O.C.	
		Indexes, 1980 = 100																	
		Perf.	Lead.	Perf.	Lead.	Perf.	Lead.	Perf.	Lead.	Perf.	Lead.	Perf.	Lead.	Perf.	Lead.	Perf.	Lead.	Perf.	Lead.
July	85	110	117	108	117	106	121	113	127	97	110	103	119	117	119	112	127	125	148
Aug.	85	111	117	109	118	106	122	113	128	97	111	102	120	117	118	112	128	124	148
Sept.	85	110	118	109	118	106	123	113	128	97	111	101	121	117	119	113	126	124	151
Oct.	85	110	117	109	119	107	123	114	127	97	111	101	122	117	120	114	125	126	152
Nov.	85	111	117	110	119	107	124	115	128	97	111	102	122	117	119	115	124	126	153
Dec.	85	112	118	110	119	106	123	114	128	97	112	101	124	117	118	115	123	127	156
Jan.	86	112	119	111	119	108	122	115	128	98	112	102	125	118	119	116	123	130	156
Feb.	86	112	120	111	121	108	122	115	128	98	112	102	126	118	116	115	122	132	158
Mar.	86	112	119	111	120	108	123	115	130	98	112	102	127	118	117	115	119	133	161
Apr.	86	113	120	112	121	110	125	116	132	98	111	102	129	118	120	116	120	132	162
May	86	112	120	111	121	109	126	116	133	98	111	104	130	118	121	116	120	133	164
June	86	112	120	111	121	111	127	116	133	98	111	103	129	118	123	117	122	133	165
July	86	113	120	111	122	111	126	117	134	98	112	104	129	118	124	116	122	135	167
Aug.	86	113	120	111	122	111	127	118	136	98	111	102	130	117	124	116	122	136	169
Sept.	86	114	123	112	122	112	127	118	138	99	113		132	118	126	116	125	136	170
Oct.	86	114	123															138	173
		Growth Rates, Percent																	
July	85	2	2	4	5	7	7	4	6	3	0	5	7	4	6	8	15	-1	6
Aug.	85	3	3	4	6	6	7	4	6	2	0	2	7	3	3	8	15	-2	5
Sept.	85	3	5	4	5	6	7	3	5	2	0	1	7	3	4	8	11	-1	8
Oct.	85	2	2	4	5	6	7	4	4	2	-1	0	7	2	4	8	7	2	10
Nov.	85	3	1	4	5	5	7	6	4	2	0	1	6	2	2	9	3	1	10
Dec.	85	4	4	5	5	3	4	4	3	2	1	0	8	2	0	7	0	2	12
Jan.	86	4	4	5	4	5	3	5	3	2	1	0	8	2	0	9	0	7	10
Feb.	86	3	5	4	5	4	1	4	2	2	1	1	10	2	-4	5	-2	8	12
Mar.	86	2	3	3	4	4	3	4	5	2	1	2	10	2	-2	5	-7	10	13
Apr.	86	4	4	4	4	7	5	4	7	2	0	1	12	2	2	4	-6	7	13
May	86	2	3	3	3	5	6	4	7	1	-1	3	11	1	4	4	-6	8	13
June	86	2	3	2	3	7	6	4	7	2	-1	2	9	1	7	5	-2	7	13
July	86	3	3	1	3	7	4	4	8	1	1	4	7	0	8	2	-2	9	13
Aug.	86	3	1	1	3	6	4	4	9	2	0	-1	7	-1	7	1	-1	9	14
Sept.	86	3	6	1	3	6	4	4	11	2	4		8	1	9	1	3	8	13
Oct.	86	3	6															10	14
		Ten Year Annual Growth Rate, Percent																	
1969-79		3	3	4	4	3	3	4	4	3	3	2	2	5	5	4	4	10	10

		9 Countries		8 Countries ex. U.S.		North America (2)		Europe (4)		Pacific Region (3)	
		Indexes, 1980 = 100									
		Perf.	Lead.	Perf.	Lead.	Perf.	Lead.	Perf.	Lead.	Perf.	Lead.
July	85	110	119	109	120	110	117	105	120	117	121
Aug.	85	110	119	109	120	110	117	105	121	116	120
Sept.	85	110	120	109	121	110	118	105	121	117	120
Oct.	85	110	120	110	121	110	117	105	121	117	121
Nov.	85	110	119	110	121	111	117	106	122	117	121
Dec.	85	111	120	110	121	112	118	106	122	117	120
Jan.	86	111	120	111	121	112	119	106	122	118	120
Feb.	86	111	120	111	120	112	120	106	122	118	118
Mar.	86	111	120	111	122	112	119	107	123	118	119
Apr.	86	112	122	112	123	113	120	108	124	118	121
May	86	112	122	112	124	112	120	108	125	118	122
June	86	112	123	112	125	112	120	108	125	118	124
July	86	112	123	112	125	113	120	109	125	118	125
Aug.	86	112	123	112	126	113	120	108	126	117	125
Sept.	86	113	125	112	127	113	122	109	128	118	127
		Growth Rates, Percent									
July	85	4	4	5	6	3	3	5	5	5	7
Aug.	85	4	4	4	5	3	3	4	5	4	5
Sept.	85	3	5	3	5	3	5	3	5	3	4
Oct.	85	3	4	3	5	2	3	4	4	3	5
Nov.	85	3	3	4	4	3	2	4	4	3	3
Dec.	85	3	3	3	3	4	4	3	4	2	1
Jan.	86	4	3	3	2	4	4	3	3	3	1
Feb.	86	3	2	3	1	3	5	3	3	3	-3
Mar.	86	3	2	3	2	2	3	3	4	2	-2
Apr.	86	4	4	3	4	4	4	4	5	2	1
May	86	3	4	3	5	2	3	3	6	2	4
June	86	3	4	3	5	2	3	4	5	2	6
July	86	3	4	3	5	2	3	4	5	1	7
Aug.	86	2	4	2	6	3	1	3	5	-1	6
Sept.	86	3	7	3	7	3	5	4	7	1	8
		Ten Year Annual Growth Rate, Percent									
1969-79		4	4	4	4	3	3	3	3	5	5

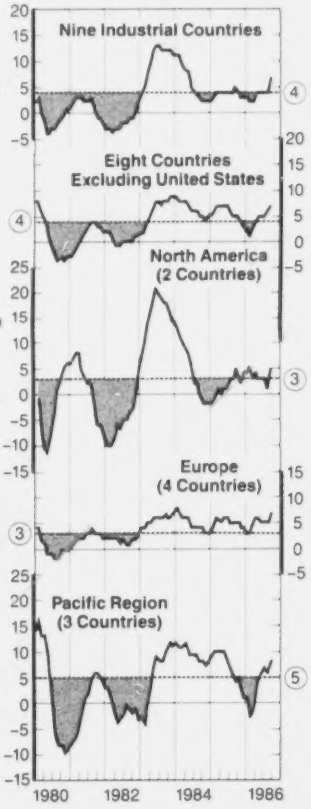
Where We Are

Growth Rates, %, Performing Indexes



Where We're Headed

Growth Rates, %, Leading Indexes



Note: Horizontal dashed lines are average growth rates for 1969-79 in the index and in real GNP
Sources: CIBCR and The Conference Board